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Supreme Court of the United States

October Term,

No. 317

LEO P. McKEE, as Trustee for INDUSTRIAL FINANCE CORP., ET AL.,

Petitioner,

versus

GREAT AMERICAN INSURANCE COMPANY,

Respondent.

LEO P. McKEE, as Trustee for INDUSTRIAL FINANCE CORP., ET AL.,

Petitioner,

versus

AMERICAN CASUALTY COMPANY OF READING, PENNSYLVANIA,

Respondent.

Petition for Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit.

CARL V. WISNER, JR.
Attorney for Petitioner
201 Southeast Second Street
Fort Lauderdale, Florida

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PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

To: The Honorable, the Chief Justice and the Associate Justices of the Supreme Court of the United States:

Now on this day comes Leo P. McKee, as trustee in bankruptcy for Industrial Finance Corporation and Commercial Capital Corporation, bankrupts, and brings this his petition for a writ of certiorari to the Court of Appeals for the Fifth Circuit, and in support thereof would show:

REFERENCE TO OPINIONS BELOW

By this petition, pursuant to Rule 23, par. 5, of the Rules of this Court, petitioner seeks a review of two decisions of the Fifth Circuit Court of Appeals. The opinion in the first of said cases, involving Great American Insurance Company as the respondent, has been informally reported in Vol. 2 of the Advance Sheets for 316 F.2d, at page 473; the second involving American Casualty Company of Reading, Pennsylvania, as the respondent, has been informally reported in Vol. 2 of the Advance Sheets for 316 F.2d, at page 428. Copies of these opinions are appended to this petition as Appendices A and B.

STATEMENT OF JURISDICTIONAL GROUNDS

1. Judgments affirming the District Court for the Southern District of Florida, were entered April 29, 1963, by the Fifth Circuit Court of Appeals.

2. It is submitted that Sec. 2101(c), Judicial Code (28 U.S.C. Sec. 2101), confers jurisdiction on this court to review the judgments in question.

THE QUESTIONS PRESENTED FOR REVIEW

The following questions are presented for review:

1. Under the law of Florida can a corporate debtor "pierce the corporate veil" to assert an alleged defense arising out of activities of corporate officers.

2. In an action on a commercial blanket bond does a trustee in bankruptcy for a corporation insured under the bond have "no more rights than the bankrupt itself".

3. Can a district court in a summary hearing and without trial, determine that as a matter of law an alter ego status exists between a bankrupt corporation and one of its officers, directors and stockholders.

Jurisdiction of the district court was based on Sec. 1332, Judicial Code (28 U.S.C. 1332).

* * * * *

In respect of the first of the questions, petitioner submits that the decisions of the court below are contrary to the applicable law of the State of Florida, **Riley vs. Fatt**, 47 So. 2d 769, and its own cases of **Maule Industries, Inc. vs. Gerstel**, 232 F.2d 294, 297, and **Coryell vs. Phipps**, 128 F.2d 702, 704, affirmed by this court, 317 U.S. 406.

In respect of the second of the questions, the decisions of the court below are in conflict with applicable decisions in the Fourth Circuit Court of Appeals, **Levey vs. Jamison**, 82 F.2d 958, and its companion case, **In re**

Schluter Green & Co., 93 F.2d 810, and in contravention of its own decisions as applied to a receiver for an insolvent savings and loan association, **American Employers Insurance Company vs. Franklin Savings & Loan Co.**, 89 F.2d 224, and the companion case **Franklin Savings & Loan Co. vs. American Employers Insurance Co.**, 99 F.2d 494.

Further, as to this phase, the Fifth Circuit Court of Appeals has said,

> "The trustee is, of course, a successor of the bankrupt for many purposes. But he is much more both in the extraordinary rights with which the Bankruptcy Act invests him and as a general representative of the creditors." **Coleman vs. Alcock**, 272 F.2d 618, 621-622.

In respect of the third question, a leading case in the Federal Courts on the subject of establishing the status of alter ego is the Tenth Circuit Case of **Fish vs. East**, 114 F.2d 177, in which the court particularly points out, page 191, 114 F.2d, that the determination of the status of alter ego "is primarily a question of fact and degree". Thus, in holding as a matter of law that an alter ego status existed, the decision of the court was clearly erroneous.

ARGUMENT

Note: In all references to the records below, the docket numbers of the case follow the page designation to differentiate the records.

(a) THE FACTS

On April 24, 1959, Robert A. McKee (there is no familial or other relationship between Robert A. McKee and petitioner, Leo P. McKee, the trustee in bankruptcy) activated Commercial Capital Corporation with offices in St. Petersburg, Florida. His purpose was to create a so-called "eight-percenter", in which the corporation borrowed money from the public on notes maturing within a year, paying interest monthly at an eight percent annual rate. The corporation was insolvent within the meaning of Sec. 1(19) of the Acts of Congress relating to bankruptcy and had creditors from the date of its activation to the date of the filing of the petition. (Rec. 7, 19954).

September 29, 1959, respondent, American Casualty Company of Reading, Pennsylvania, issued its commercial blanket bond No. 903,434 to the bankrupt Commercial Capital Corporation in an amount of $100,000. (Rec. 15-21, 19954). This bond was cancelled January 27, 1960, but during its effective period, defalcations of Robert A. McKee and others in the amount of $46,585.14 occurred.

On September 7, 1959, Robert A. McKee organized Industrial Finance Corporation to further his eight percenter enterprise on the East Coast of Florida. It likewise, was insolvent and had creditors from the date of its organization to the date the bankruptcy petition was filed. (Rec. 5, 19940). On the date of cancellation of the $100,000 commercial blanket bond of the respondent, American Casualty Company of Reading, Pennsylvania, January 27, 1960, the respondent, Great American Insurance Company, in case No. 19940 below, executed and delivered its commercial blanket bond, No. 8,046,540, in the amount of

$100,000. This bond was cancelled June 28, 1961, by the respondent (Rec. 49, 19940), because Robert A. McKee had been telling his "investors" that the bond in suit was issued by the respondent to protect their investments in the bankrupt Industrial Finance Corporation and Commercial Capital Corporation.

The premiums on both bonds in suit were paid by the bankrupt corporations and not by Robert A. McKee. (Rec. 2, 19940, Rec. 5, 19954). The bond of respondent, American Casualty Company of Reading, Pennsylvania, was issued to Commercial Capital Corporation; the bond of respondent, Great American Insurance Company was issued with the curious nomenclature for the obligee, "Robert A. McKee, d b a Industrial Finance Corporation and Commercial Capital Corporation." (Rec. 21, 19940).

During the effective period of the bond of the respondent, Great American Insurance Company, McKee and his confederates abstracted $267,720.87 from the funds of the two bankrupts.

(b) THE DECISIONS BELOW

In the case involving the respondent, American Casualty Company of Reading, Pennsylvania, notwithstanding the circumstances that the premiums on the bond were paid by the bankrupt Commercial Capital Corporation, the court held that

> "Robert A. McKee, the principal officer and sole stockholder who perpetrated the fraud, **as a matter of law** was the alter ego of the obligee-bankrupt." (Emphasis ours)

The court further held that McKee's knowledge of the frauds was imputed to the bankrupt and, notice not having been given within ninety days after the imputed discovery, the suit could not be maintained.

The court went on to say:

> "The fact that McKee took the corporation's money does not insulate it from the knowledge he possessed since there was no adverse interest between McKee and the corporation wholly owned by him."

The record shows (Rec. 7, 19954) that there were one-half million dollars of noteholders between McKee and the corporation during the effective period of the bond.

In the Great American Insurance Company case, the court below took the position that, notwithstanding the facts that (a) Industrial Finance Corporation had paid the premiums on the bond, (Rec. 2, 38, 19940), (b) the agent for the surety company was responsible for the nomenclature of the obligee as "Robert A. McKee d b a Industrial Finance Corporation and Commercial Capital Corporation," (Rec. 41-42, 19940) and (c) the bond in suit identified Robert A. McKee as one of the employees covered (Rec. 54, 19940), and held that the trustee could not maintain the action.

(c) ARGUMENT

Robert A. McKee set up two corporations of which for the major portion of the time here in question, he was the sole stockholder, borrowed approximately a mil-

lion dollars from the public, and went bankrupt. The first of the bonds in suit was applicable only to the first created corporation, was effective for a short period, during which abstractions of $46,585.14 within the terms of the coverage of the bond occurred. On the date of cancellation of that bond, a second bond was issued by respondent, Great American Insurance Company, covering both bankrupt corporations, effective from January 27, 1960, to June 26, 1961, during the effective period of which abstractions of $267,720.87 within the terms of coverage of the bond occurred.

As to the first bond, the court below has held that **as a matter of law** Robert A. McKee was the alter ego of the obligee-bankrupt, that his knowledge of his own defalcations was imputed to the obligee-bankrupt, that the trustee had no more rights than the bankrupt, and could not maintain the suit.

Of this we say first that, under the law of Florida which is applicable, only a creditor can pierce the corporate veil, **Riley vs. Fatt,** 47 So. 2d 769; Cf. **Maule Industries, Inc., vs. Gerstel,** (5th Cir.) 232 F.2d, 294, 297; **Coryell vs. Phipps,** (5th Cir.) 128 F.2d 702, 704, affirmed 317 U.S. 406; and this remedy is not afforded debtors such as the obligors on these bonds. Second, that the alter ego status is primarily a question of fact. It cannot be determined in summary proceedings but only after a trial. Cf. **Fish vs. East,** (10th Cir.) 114 F.2d 177. This is the more true since the complaint in each of the suits alleges, par. 8 f., 19940 (Rec. 7, 19940), par. 7 e., 19954 (Rec. 8, 19954):

> "That at all times during the effective date of the bond, the said Robert A. McKee was an

employee of one or the other of the plaintiff's bankrupts, and the transfers by him made, herein complained of, were made by him as such an employee and not as an officer, director or stockholder of one or the other of the plaintiff's bankrupts;"

Finally, in reaching the conclusion that it did, the court below relied on its own decision in **Franklin Savings & Loan Company vs. American Employers Insurance Company**, (5th Cir.) 99 F.2d 494, which holds exactly to the contrary. The cited case dealt with a receiver for a building and loan association and permitted the receiver to recover on a commercial blanket bond for defalcations caused by the activities of the president and principal officer of the insolvent association. While the surety urged that knowledge of the defalcations was imputed to the corporation, the court refused so to do, 99 F.2d at page 497.

In the Great American Insurance Company case, the court below relied solely on the nomenclature of the bond, notwithstanding the circumstance that the party responsible for the nomenclature was the agent of the obligor (Rec. 41-42, 19940), that Robert A. McKee was identified in the bond application as a covered employee, and the bankrupt Industrial Finance Corporation paid the premium on the bond.

SUMMARY

The case is of importance to Floridian investors who have almost a million dollars at stake in the two bankrupts. In the instance of the Great American Insurance Company bond, Robert A. McKee deliberately used the existence of the bond as an argument in the sale of his "securities", representing in effect that the bond was issued to insure their safety.

It is further respectfully submitted, that the statements of the court below in 316 F.2d 428, at page 429,

> ". . . the principal officer and sole stockholder who perpetrated the fraud, as a matter of law was the alter ego of the obligee-bankrupt, . . ."

and the further statement at page 430 of 316 F.2d,

> ". . . the trustee who has no more rights than the bankrupt itself, may not maintain the suit."

are clearly contrary to law, and in the future will rise to plague litigants and the courts if they are not corrected by the action of this court.

All of which is respectfully submitted.

CARL V. WISNER, JR.
Attorney for Petitioner
201 Southeast Second Street
Fort Lauderdale, Florida

APPENDIX A

IN THE
UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

No. 19940

LEO P. McKEE, as Trustee for INDUSTRIAL FINANCE CORPORATION, ET AL.,

Appellants,

versus

GREAT AMERICAN INSURANCE COMPANY,

Appellee.

Appeal from the United States District Court for the Southern District of Florida.

(April 29, 1963)

Before TUTTLE, Chief Judge, JONES and BELL, Circuit Judges.

PER CURIAM: It appearing that the plaintiff-trustee is suing the obligor on a commercial blanket bond covering loss sustained by the insured through fraudulent or dishonest acts committed by any of the insured's employees, and it appearing further that the bond issued to the principal officer and sole stockholder of the two

bankrupt companies (in favor of "Robert A. McKee [no relation to the trustee in bankruptcy] d b a Industrial Finance Corporation and Commercial Capital Corporation") for whom the plaintiff is the trustee in bankruptcy, and it appearing further that the fidelity losses the trustee sues upon were occasioned by the fraudulent acts of Robert A. McKee, we conclude, as did the district court in granting the defendant's motion for summary judgment, that the bonds did not cover the defalcations of Robert A. McKee, the principal officer and sole stockholder of the corporations.

The judgment is hereby

AFFIRMED.

A true copy

Test: EDWARD W. WADSWORTH
Clerk, U. S. Court of Appeals,
Fifth Circuit

By CLARA R. JAMES
Deputy

New Orleans, Louisiana
July 17, 1963

APPENDIX B

IN THE

UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

No. 19954

LEO P. McKEE, as Trustee for INDUSTRIAL FINANCE CORP., ET AL,
Appellants,

versus

AMERICAN CASUALTY COMPANY OF READING, PENNSYLVANIA,
Appellee.

Appeal from the United States District Court for the Southern District of Florida.

(April 29, 1963)

Before TUTTLE, Chief Judge, JONES and BELL, Circuit Judges.

PER CURIAM: It appearing that the trustee in bankruptcy is suing the obligor on a commercial blanket bond issued to the trustee's bankrupt, the obligee under

the bond, and it appearing that the bond covered any losses sustained by the plaintiff's bankrupt through any dishonest, fraudulent or criminal act of any of the employees of the bankrupt, which losses are sustained while the bond is in force and discovered by the obligee within twelve (12) months after the bond is cancelled, and further that liability only attaches if the obligee has notified the obligor within 90 days of discovering the loss, it appearing further that the fidelity losses involved were occasioned by the fraudulent acts of Robert A. McKee (no relation to the trustee), the "sole stockholder and the dominant factor in its (the bankrupt corporation) operation during the effective period of the bond," (language of the complaint) it appearing further that the trustee notified the defendant only after the expiration of 18 months from the termination date of the bond (approximately the date the trustee was appointed), and it appearing that the trustee did not notify the surety within 90 days of the alleged date of discovery, we conclude:

That the obligee under the bond, the bankrupt, had "discovered" the loss within the twelve months' period by reason of the fact that Robert A. McKee, the principal officer and sole stockholder who perpetrated the fraud, as a matter of law was the alter ego of the obligee-bankrupt, and that no notice having been given within 90 days after this imputed discovery by the obligee, the trustee who has no more rights than the bankrupt itself, may not maintain the suit. The fact that McKee took the corporation's money does not insulate it from the knowledge he possessed since there was no adverse interest between

McKee and the corporation wholly owned by him. Cf. **Franklin Savings & Loan Co. v. American Employees Ins. Co.**, 5 Cir., 99 F. 2d 494. Furthermore, we find that by the plaintiff's own allegations the "discovery" did not occur until after the expiration of the allowable twelve months' period, so that the trustee is precluded by the first condition precedent to maintaining an action on this bond.

The judgment is

AFFIRMED.

A true copy

Test: EDWARD W. WADSWORTH
Clerk, U. S. Court of Appeals,

By CLARA R. JAMES
Deputy

New Orleans, Louisiana
July 17, 1963